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CHARLES ELMORE CROPLEY

IN THE

Supreme Court of the United States

OCTOBER TERM 1945

No. 1086

JULES E. PICCARD, on behalf of himself and for the benefit of and on behalf of the defendant, The Sperry Corporation, and all other stockholders of said defendant, The Sperry Corporation, who may be similarly situated,

Petitioner,

against

THE SPERRY CORPORATION, STANDARD CAPITAL COMPANY, J. CHEEVER COWDIN, THOMAS A. MORGAN, EDWARD ALLEN PIERCE, individually and as directors and voting trustees, etc., ALEXANDER B. ROYCE and JOHN SANDERSON, individually and as directors, etc., THOMAS B. DOE, individually and as officers, etc., and J. RUSSELL FORGAN, WRIGHT DURYEA and others, individually and as partners trading under the firm name and style of FIELD GLORE & COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF

A. JOSEPH GEIST,
Solicitor for Petitioner.

Of Counsel:
GEORGE E. NETTER,
HELEN M. WOLFSOHN.

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No.

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THE SPERRY CORPORATION, STANDARD CAPITAL COMPANY, J. CHEEVER COWDIN, THOMAS A. MORGAN, EDWARD ALLEN PIERCE, individually and as directors and voting trustees, etc., ALEXANDER B. ROYCE and JOHN SANDERSON, individually and as directors, etc., THOMAS B. DOE, individually and as officers, etc., and J. RUSSELL FORGAN, WRIGHT DURYEA and others, individually and as partners trading under the firm name and style of FIELD GLORE & COMPANY,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully shows:

Statement

This is a petition for a writ of certiorari to review a determination of the United States Circuit Court of Appeals for the Second Circuit, unanimously affirming a judgment of the United States District Court for the Southern

District of New York, dismissing the complaint upon the merits as to all defendants other than the nominal defendant The Sperry Corporation, after trial before Mr. Justice Rifkind without a jury.

This is a stockholders' derivative suit brought for the benefit of defendant The Sperry Corporation.

Facts

Defendants, Field Glore & Company, stock brokers and members of the New York Stock Exchange, were desirous of getting an option on a large and valuable block of Curtiss-Wright Corporation Class A and Common Stock owned by The Sperry Corporation.

Defendant Cowdin was a director and voting trustee of The Sperry Corporation, by whom he was employed at a salary of $1,000 per month "in representing the interests of this corporation in respect to its investment in the Curtiss-Wright Corporation" (2313-2315).* Field Glore asked Cowdin why they could not get the business of disposing of The Sperry Corporation's holding of Curtiss-Wright, particularly urging upon him that Field Glore be given an option to purchase the stock (629-631, 636-637, 653, 662, 1240-1242).

Cowdin is the dominant stockholder and president, director and voting trustee of defendant Standard Capital Company, a corporation formed and promoted by him to engage in the business of financing motion pictures (430-431, 973-999, 1358-1375).

This action is based upon the admitted fact that Field Glore agreed to give to Cowdin's company, Standard Capital, fifty percent of the substantial profits resulting to Field Glore from the option which Cowdin procured for that firm from The Sperry Corporation. Cowdin alone acted for Sperry in negotiating this option with Field

* Numerals in parenthesis refer to folios in the Record unless otherwise indicated.

Glore (449, 1282-1283). The option agreement is Exhibit 6 in evidence (2225-2239).

The actionable breach of fiduciary duty on Cowdin's part and his misrepresentation to his fellow directors with respect to his company's fifty percent interest in Field Glore's profits were found by the District Judge (2615, 2632).

Before procuring the option for Field Glore, Cowdin had obtained for them an order from The Sperry Corporation to sell 90,000 shares of Class A Curtiss-Wright stock at a minimum price of $10 a share (2318); but no stock was sold pursuant to this order as the market price never reached $10 a share before the order was replaced by the option in September, 1935 (2628; Finding No. 21). Theretofore all sales of Curtiss-Wright stock by Sperry had been made through the brokerage firm of E. A. Pierce & Co. (739, 779, 1021).

It was while Field Glore & Company were brokers under the said selling order that they arranged with Cowdin to change the selling order to an option to Field Glore to purchase and to give Cowdin's company, Standard Capital, fifty percent of their profits resulting from that option (660, 693, 1273-1277, 1544-1545, 2215; Ex. 3).

Cowdin told his fellow directors that a company in which he and Armsby, also a director of Sperry, were interested as stockholders and directors would receive from Field Glore a participation in any profits resulting from the option. The Trial Judge found that the language Cowdin used conveyed to the directors the understanding that the participation would be a small one and that he knew such was their understanding. Neither Cowdin nor the other directors regarded a fifty percent participation as a small one. None of the directors inquired and Cowdin did not disclose the name of the company to share in the profits nor the extent of its share (2632-2633; Findings of Fact Nos. 26 and 27). Sperry's officers and directors made no inquiry whatsoever with respect to this participation, either as to its size, or the reason for it, the name of the

company or the extent of Cowdin's interest in the company (805-807, 1034, 1958-1961, 1535).

Although counsel for Field Glore discussed with counsel for Sperry the fact that Standard Capital, the company in which Cowdin was interested, was to receive a participation in the profits of Field Glore, they did not mention that the participation was to be as much as fifty percent, nor did they mention that Cowdin was president of Standard Capital, and Sperry's counsel did not ask the extent of the participation or the consideration for it (1529-1531, 1537, 1541-1542). Field Glore made no disclosures to The Sperry Corporation, its officers or directors.

Field Glore exercised the option and resold the stock, realizing a total profit of $528,735.65, exclusive of commissions of $66,686.56 to Field Glore (2252-2253, 543-544). Field Glore paid Sperry $140,864.08 as the share of the profits to which it was entitled under the terms of the option agreement (2250-2253). The remaining profit of $387,871.57 was divided equally between Field Glore and Cowdin's company, $193,935.79 to each (2265-2273).

While the option to Field Glore was in existence, defendant Morgan, president, director and voting trustee of The Sperry Corporation, was induced by Cowdin to invest $5,000 in the stock of Standard Capital (1358-1365, 828). Through Cowdin, the wife of Sperry's vice-president, treasurer and director, Sanderson, also invested $5,000 in the stock of Standard Capital while the option was in existence (1358-1365, 829).

Morgan and Mrs. Sanderson, as well as Cowdin and Armsby, were thus interested in Standard Capital when Sperry's directors purported to authorize a settlement with Cowdin and Standard Capital.

Holding of the District Court

The opinion of the District Judge is reported in 48 Fed. Supp. 465.

The District Court concluded as a matter of law that there was no fiduciary relationship between Field Glore and The Sperry Corporation (2663; Conclusion of Law 6), and that Field Glore executed the option agreement in good faith and in the reasonable belief that the facts concerning the participation of Standard Capital had been disclosed to and approved by the directors of Sperry (2663; Conclusion of Law 7).

The District Court also concluded as a matter of law that the directors and officers of Sperry, other than Cowdin and Armsby, did not commit acts of waste or negligence or bad faith in approving the option agreement with Field Glore or in approving a small participation on the part of Standard Capital in the profits accruing to Field Glore out of said option agreement (2661-2662; Conclusions of Law 2 and 3).

The District Judge held that the releases subsequently given to Cowdin and Standard Capital by the same directors of Sperry who had approved the option without any inquiry about the participation in the profits by Cowdin's company, were valid and barred the action against them. This holding depends upon a holding that the releases and the settlement pursuant to which they were given were properly authorized by the valid action of a proper quorum of Sperry's directors (2596-2598, 2611, 2614).

In this connection the Court considered the provision of the Sperry charter to the effect that interested directors may be counted when present at meetings of board of directors for the purpose of determining the existence of a quorum. In what the Court considered to be an absence of controlling Delaware authority, it held that a Federal Court should not assume such charter provision to be contrary to the law of Delaware, the state of Sperry's incorporation (2610-2611).

Decision of the Circuit Court of Appeals, Second Circuit

The opinion of the Circuit Court of Appeals is reported in 152 Fed. (2d) 462. That Court unanimously affirmed the Court below, with a short per curiam opinion in which it said:

> "* * * In so far as the appeal raises questions of fact we think the findings of the trial judge are supported by the evidence; in so far as it involves questions of law we agree with his disposition of them. The judgment is affirmed on the opinion below, 48 F. Supp. 465."

Jursidiction of this Court

The decree of the Circuit Court of Appeals was entered on January 10, 1946. The jurisdiction of this Court is under Judicial Code, Section 240a, as amended (28 U. S. C. A. Sec. 347a).

Questions Involved

There was only one question of fact in this case upon which there was any conflict in the evidence, namely, whether Cowdin represented to his fellow directors that the participation in Field Glore's profits by a company in which he was interested would be a small one. The District Court has resolved that question of fact against Cowdin, and the Circuit Court of Appeals has affirmed that finding (2632; Finding No. 26) with which petitioner is not in disagreement. No disputed question of fact remains in the case.

The principal questions involved are:

1. What was the standard of duty of Field Glore in dealing with Sperry's director and sole agent, Cowdin, and

in agreeing to share equally with him through his company, Standard Capital, the profits from the option procured through him? Was not Field Glore, at the very least, under a positive duty, at its peril, to make certain that unequivocal and complete disclosure of the fifty percent participation in its profits by Cowdin's company was made to The Sperry Corporation? The Courts below have held that there was no such duty on Field Glore.

2. Were the Courts below correct in holding that there was no fiduciary relationship between Field Glore and Sperry?

3. Could Field Glore terminate their fiduciary duties as brokers by entering into an agreement with Sperry's other fiduciary, Cowdin, in conflict with their principal's interest, and without fully and unequivocally disclosing to Sperry all the facts and circumstances?

4. Did the directors of The Sperry Corporation act properly in failing to make inquiry as to the extent or reason for the participation in Field Glore's profits by Cowdin's company when they were put on notice that a company in which Cowdin was interested would share in such profits?

5. Did the Courts below err in holding that the provision of Sperry's charter permitting interested directors to be counted towards a quorum is not invalid under the law of Delaware, the state of Sperry's incorporation?

6. Did the Courts below err in failing to ascertain the law of the State of Delaware from all the available data and to apply it?

Reasons Why Writ Should Be Granted

(A) The Courts below have erroneously decided important questions of local law in a manner which is in conflict with established legal principles and decisions.

The high standards to which courts of equity have heretofore unswervingly held fiduciaries and those dealing with them are a cornerstone of the nation's structure of large corporate business and finance, and no elaboration is needed to show the extreme public importance of any decision which even tends to erode that cornerstone.

The decisions below seriously impaired the fiduciary principle of undivided loyalty to which courts of equity, both state and federal, have always adhered for the protection of corporations and others who act through agents.

The decisions below permit one dealing with a corporation through its agent to share the resulting profits of the transaction equally with the corporation's agent, without placing upon the person so dealing with the agent any duty to see to it that the facts are fully disclosed to the principal.

The seriousness of this holding is aggravated by the fact that Field Glore was a broker under the selling order and hence itself in a fiduciary relationship to Sperry when it agreed to share equally with Sperry's sole agent the profits which would result from changing that selling order to Field Glore as broker into an option to Field Glore to purchase.

Established principles of law and equity are violated by the holding below that there was no fiduciary relationship between Field Glore and Sperry.

In holding valid under Delaware law the provision of Sperry's Charter permitting interested directors to be counted towards a quorum, the decisions below seriously breach the structure erected by courts of equity to confine within proper bounds the conduct of fiduciaries, and have given judicial sanction to a device for evading fiduciary

obligations. This holding is contrary to the universal rule and is contrary to Delaware law as ascertainable from all the available data.

(B) The Courts below have erroneously decided an important question of Federal law contrary to the decisions of this Court.

In the absence of a direct holding on the question by a Delaware Court, it was the duty of the District Judge under the decisions of this Court to ascertain from all the available data the Delaware law as to the validity or invalidity of the Sperry Charter provision purporting to authorize an interested director to be counted towards a quorum and to apply the Delaware law as so ascertained by him.

Instead, the District Judge merely held that he would not assume that the charter provision was contrary to the public policy of Delaware. The Circuit Court of Appeals has affirmed this holding.

WHEREFORE, your petitioner respectfully prays that this petition for a writ of certiorari be granted to review the aforesaid determination of the Circuit Court of Appeals for the Second Circuit.

Dated: April 8, 1946.

A. JOSEPH GEIST,
Solicitor for Petitioner.

IN THE

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No.

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Respondents.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

POINT I

Field Glore should have been adjudged liable for participating with Cowdin in the breach of his trust and should have been charged with a positive duty to see to it, at its peril, that full and frank disclosure of all the facts was made to Sperry.

Cowdin's violations of his fiduciary duties to Sperry are established by the decision below (2615, 2632; Finding No. 26).

Field Glore knew that Cowdin was a director of Sperry and was acting for it as sole agent in connection with the sale of its Curtiss-Wright stock (456-457, 564, 655, 2637; Finding No. 34). In spite of this knowledge, Field Glore agreed to pay Cowdin's company, Standard Capital, fifty percent of its profits resulting from the option to purchase procured for it by Cowdin (450-456, 599, 1312).

Field Glore did realize that the arrangements should be fully disclosed to the Sperry directors (451), but the arrangements were not fully disclosed and, as the Courts below have found, the representation which Cowdin made to Sperry was untrue (2615).

We submit that Field Glore, if it wished to split its profits with Sperry's representative, was at the very least charged with the duty of seeing to it that Sperry was fully informed, not only that Cowdin's company was receiving a participation in its profits, but that it was receiving an unusual participation of as much as fifty percent.

The option which Field Glore thus obtained through Cowdin resulted in very substantial profits which were divided between Field Glore and Cowdin's company.

In *Cahall* v. *Lofland*, 12 Del. Ch. 299, 114 Atl. 224, one who had purchased property from a corporation, employed the president of the corporation as his agent to resell part of the property. The purchaser was held liable to the corporation for the profit resulting from the resale. The Delaware Court quoted with approval the following from *Panama* v. *Indian*, 10 L. R. Ch. App. Cas. 515:

> "But on such a subject as this, there shall not only have been an absence of concealment, but full and complete disclosure and information."

In *Jackson* v. *Smith*, 254 U. S. 586, at page 589, this Court said:

> "And others who knowingly join a fiduciary in such an enterprise likewise become jointly and severally liable with him for such profits."

To the same effect see:

Restatement of the Law of Restitution, Sec. 138 (2);
Irving Trust Company v. *Deutsch* (C. C. A. 2nd), 73 F. (2d) 121, certiorari denied, 294 U. S. 708;
Wechsler v. *Bowman,* 285 N. Y. 284;
Jacobellis v. *Prudential,* 244 App. Div. 255, 279 N. Y. Supp. 44, affirmed with modification on other grounds, 269 N. Y. 632;
Public Shoe Stores v. *Goldstein* (1st Dept.), 225 App. Div. 350, 233 N. Y. Supp. 73;
Mannaberg v. *Herbst,* 45 N. Y. Supp. (2d) 197, aff'd 267 App. Div. 818, 47 N. Y. Supp. (2d) 100, aff'd 293 N. Y. 657.

"We are told that the conflict of interest was sufficiently revealed when the brokers informed the plaintiff that the sale was to be made to a client of their office. Disclosure so indefinite and equivocal does not set the agent free to bargain for his own account or for the account of a corporation which acts through him alone. If dual interests are to be served, the disclosure to be effective must lay bare the truth, without ambiguity or reservation, in all its stark significance (*Dunne* v. *English,* L. R. 18 Eq. 524; *Imperial Merc. Credit Assn.* v. *Coleman,* L. R. 6 H. L. 189)." *Wendt* v. *Fischer,* 243 N. Y. 439, at p. 443.

Field Glore knew that its true arrangement with Cowdin was one which the Sperry directors, who were themselves fiduciaries, should not and could not approve.

In *Landes* v. *Hart* (1st Dept.), 131 N. Y. App. Div. 6, at page 7, 115 N. Y. Supp. 337, it is said:

"An agreement which is designed, or which in its nature and effect tends to lead persons who are charged with the performance of trusts or duties for the benefit of others to violate or betray them, is contrary to public policy and void and cannot be enforced. (*Bliss* v. *Matteson,* 52 Barb. 335, aff'd 45 N. Y. 22; *Moss* v. *Cohen,* 11 Misc. Rep. 184; *West* v. *Camden,* 135 U. S.

507; *Barkley* v. *Williams*, 26 Ill. App. 213.) Such a contract with a third person is not made valid although the acts of the unfaithful agent may have in fact resulted in benefit to his principal (*Lum* v. *McEwen*, 56 Minn. 278); *nor by the fact that the unfaithful director of a corporation informed his codirectors of his corrupt bargain.* (Munson v. S. G. & C. R. R. Co., 103 N. Y. 59, 74.)" (Italics supplied.)

See, also:

Hubbard v. *New York, N. E. & W. Investment Co.* (C. C. Mass.), 14 Fed. 675, aff'd 119 U. S. 696;

Keenan v. *Eshleman*, 23 Del. Ch. 234, 2 Atl. (2d) 904.

POINT II

The Courts below have erroneously held that there was no fiduciary relationship between Field Glore and Sperry; whereas Field Glore was in a fiduciary relationship to Sperry and is liable for the breach of its fiduciary obligations.

It was held below as a matter of law that there was no fiduciary relationship between Field Glore and Sperry (2663; Conclusion of Law 6).

At the suggestion of Cowdin, Sperry gave Field Glore, as stock brokers, an order to sell 90,000 shares of A stock at $10 a share (776-782, 1251-1252, 2209-2214; Exs. 1, 2). As stock brokers under this selling order, Field Glore were fiduciaries of their customer and principal, Sperry.

See:

McMann v. *Securities & Exchange Commission* (C. C. A. 2nd), 87 F. (2d) 377, 378;

Johnson v. *Winslow*, 155 Misc. 170, 279 N. Y. Supp. 147, aff'd without opinion 246 App. Div. 800, 285 N. Y. Supp. 1075, aff'd without opinion 272 N. Y. 476;

Taussig v. *Hart*, 49 N. Y. 301 and same case 58 N. Y. 425;
Conkey v. *Bond*, 36 N. Y. 427.

Field Glore immediately began through Cowdin to attempt to change its selling order as broker into an option to itself to purchase (636-637, 646, 656) and finally succeeded (445-448, 1291, 2225-2238; Exhibit 6, 2327-2330). As a fiduciary, Field Glore owed to its principal, Sperry, unequivocal and full disclosure that Sperry's representative in the negotiations, Cowdin, was to receive fifty percent of the profits resulting from changing that selling order into an option.

See:

Comments a and f to Section 390 of the *Restatement of the Law of Agency;*
Brown v. *Post*, 1 Hun 303, aff'd on opinion below 62 N. Y. 651;
Moffat v. *Gerry Estates, Inc.* (1st Dept.), 259 App. Div. 403, 19 N. Y. Supp. (2d) 579;
Franklin v. *Mortgage Guaranty & Security Co.* (C. C. A. 9th Cir.), 57 Fed. (2d) 834, at p. 835;
Anglo Eastern Trading Co., Inc. v. *New Tread Tire Company* (1st Dept.), 222 App. Div. 475, at p. 477, 226 N. Y. Supp. 532, at p. 534;
U. S. Ship Bd. E. F. Corp. v. *South Atlantic Dry Dock Co.* (C. C. A. 5th), 300 Fed. 56, at p. 61;
Wendt v. *Fischer*, 243 N. Y. 439, at p. 443;
Dunne v. *English*, L. R. 18 Eq. Cas. 524, at p. 533.

Thus, having realized very substantial profits in excess of ordinary brokerage commissions as a result of changing its selling order to an option, and in effecting such change having failed in its fiduciary obligation to make full and frank disclosure of Cowdin's participation, Field Glore is liable to account to Sperry for the resulting profits.

See:

Jackson v. *Smith*, 254 U. S. 586, at pp. 588 to 589;
Restatement of the Law of Restitution, Sec. 138;
Irving Trust Company v. *Deutsch* (C. C. A. 2nd), 73 F. (2d) 121, certiorari denied, 294 U. S. 708;
Wechsler v. *Bowman*, 285 N. Y. 284;
Wendt v. *Fischer*, 243 N. Y. 439;
Lonsdale v. *Speyer* (1st Dept.), 249 App. Div. 133, 291 N. Y. Supp. 495;
Jackson v. *Berry-Snelling Realty Co.*, 211 Ala. 174, 100 So. 111.

POINT III

The Courts below erred in holding valid under Delaware law the provision of Sperry's Charter purporting to authorize an interested director to be counted towards a quorum.

The certificate of incorporation of Sperry, a Delaware corporation, provides in paragraph "Tenth" thereof (2655-2656):

> "* * * Directors so interested may be counted when present at meetings of the Board of Directors or of such Committee for the purpose of determining the existence of a quorum.. Any director whose interest in any such contract or transaction arises solely by reason of the fact that he is a stockholder, officer or creditor of such company * * * shall not be deemed interested in such contract or other transaction * * *."

The learned Court below agreed that if the quoted provision is contrary to the laws of Delaware (whether statutory law or otherwise), it is invalid (2601-2602).

State ex rel. Cochran v. *Penn-Beaver Oil Co.*, 1926, 34 Del. 81, 143 Atl. 257.

The Court below held, however, that in the absence of what he considered a controlling Delaware authority, a Federal Court should not assume the provision to be contrary to Delaware law (2610-2611), and consequently that there were valid quorums at the June 30th, 1936, and July 28th, 1936, meetings which authorized and approved the settlement with Cowdin and Standard Capital. We submit that in this the Trial Judge erred.

The law is clear that the vote of an interested director may not be counted.

> *Keenan* v. *Eshleman*, 23 Del. Ch. 234, 2 Atl. (2d) 904;
> *Cahall* v. *Lofland*, 12 Del. Ch. 299, 114 Atl. 224;
> *Boray et al.* v. *H. M. Byllesby Co. et al.* (Sup. Ct., Del.), 38 Atl. (2d) 808;
> *Italo-Petroleum Corp.* v. *Hannigan*, 40 Del. 534, 14 Atl. (2d) 401.

In *Enright* v. *Heckscher* (C. C. A. 2d), 240 Fed. 863, it is said at page 872:

> "A director whose interest in a matter disqualifies him from voting upon a resolution concerning it cannot, according to the better opinion, be counted for the purpose of ascertaining whether a quorum is present when the vote is taken. A director so qualified by personal interest loses, pro hac vice, his character as a director and so cannot be counted."

That an interested director may not be counted towards a quorum is the universal rule. See cases cited in 14a *Corpus Juris* 1854 at page 92, and 19 C. J. S., Section 749 (c) at page 94, *all holding that an interested director is disqualified from being counted towards a quorum.* The District Court in its opinion (2605) cited two cases as holding contrary, *Gumaer* v. *Cripple Creek Tunnel T. & M. Co.*, 1907, 40 Colo. 1, 90 Pac. 81, and *Buell* v. *Buckingham*, 1864, 16 Iowa 284. *Gumaer* v. *Cripple Creek Tunnel T. & M. Co.* is no longer law in Colorado, in view of the later

decisions in that State, such as *Layburn* v. *Wrape*, 72 Colo. 339, 211 Pac. 367, and *Paxton* v. *Heron*, 41 Colo. 147, 92 Pac. 15. In the Iowa case cited by the District Court, *Buell* v. *Buckingham*, the by-laws provided that a quorum should consist of the president and two other directors. The question of the ineligibility of an interested president to be counted towards a quorum when present with two non-interested directors was not discussed by the Court and apparently was not raised. It was merely held that the affirmative vote of the two non-interested directors, constituting a majority of the quorum, was sufficient.

The above cited Delaware cases show that the Courts of that state have unequivocally declared that the vote of an interested director may not be counted. There was no reason for the Courts below to assume that Delaware would depart from what is now the universal rule and differentiate between not permitting a disinterested director to vote and not permitting him to be counted towards a quorum. Both are part of the same disqualification, the director having lost his character as a director, "*pro hac vice*", as pointed out by the Circuit Court of Appeals, Second Circuit, in the *Enright* case, *supra*.

The Courts below should have held the charter provision relied on by defendants a nullity and contrary to law, and that consequently the releases to Cowdin and Standard Capital Company were not valid corporate acts of The Sperry Corporation.

POINT IV

The Courts below erred in failing to ascertain the Delaware Law from all available data and to apply that law.

The District Court held that in the absence of what it considered to be controlling Delaware authority, it would not assume that the charter provision purporting to permit

interested directors to be counted towards a quorum was void as contrary to Delaware law. The Circuit Court of Appeals, Second Circuit, has sustained this holding. In the absence of a direct holding by the highest court in Delaware, it is the duty of the Federal Court to ascertain the law of Delaware "from all the available data" and apply it. This Court so held in *West* v. *American Telephone & Telegraph Co.*, 311 U. S. 223, at p. 237.

In *Fidelity Union Trust Co.* v. *Field*, 311 U. S. 169, at page 177, this Court stated:

> "* * * but it is still the duty of the federal courts, where the state law supplies the rule of decision, to ascertain and apply that law even though it has not been expounded by the highest court of the state. * * *"

As shown in the preceding point of this brief, all the avaliable data clearly indicates that the law of Delaware is the same as the law in other states, that an interested director may not be counted towards a quorum. Therefore, had the Courts below ascertained and applied that law they would have necessarily held that the charter provision relied upon by defendants was a nullity as being in conflict with the law of Delaware, the state of Sperry's incorporation, and that consequently the purported releases given to Cowdin and Standard Capital were not valid corporate acts.

POINT V

The decisions below constitute an impairment of the broad equitable principles which have been laid down by the Courts to govern fiduciaries, and sanction and establish a precedent by which such principles may be disintegrated, eroded, or evaded by subtle or narrow distinctions, and thereby injure public interest.

In *Meinhard* v. *Salmon*, 249 N. Y. 458, Judge Cardozo said, at page 464:

> "Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions (*Wendt* v. *Fischer*, 243 N. Y. 439, 444). Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court."

In 1934 the present Chief Justice of the United States wrote (48 Harv. Law Rev., p. 8):

> "I venture to assert that when the history of the financial era which has just drawn to a close comes to be written, most of its mistakes and its major faults will be ascribed to the failure to observe the fiduciary principle, the precept as old as holy writ, that 'a man cannot serve two masters'. More than a century ago, equity gave a hospitable reception to that principle, and the common law was not slow to follow in giving it recognition. * * * The separation of ownership from management, the development of the

corporate structure so as to vest in small groups control over the resources of great numbers of small and uninformed investors, make imperative a fresh and active devotion to that principle if the modern world of business is to perform its proper function. Yet, those who serve nominally as trustees, but relieved, by clever devices, from the obligation to protect those whose interests they purport to represent, corporate officers and directors who award to themselves huge bonuses from corporate funds without assent or even the knowledge of their stockholders * * * suggest how far we have ignored the necessary implications of that principle * * * but when we know and face the facts, we shall have to acknowledge that such departures from the fiduciary principle do not usually occur without the active assistance of some member of our profession * * *."

CONCLUSION

The petition for writ should be granted.

Respectfully submitted,

A. Joseph Geist,
Solicitor for Petitioner.

Of Counsel:
George E. Netter,
Helen M. Wolfsohn.

FILED
MAY 4 1946
CHARLES ELMORE CROPLEY
CLERK

Supreme Court of the United States

OCTOBER TERM 1945—No. 1086

JULES E. PICCARD, on behalf of himself and for the benefit of and on behalf of the defendant, THE SPERRY CORPORATION, and all other stockholders of said defendant, THE SPERRY CORPORATION, who may be similarly situated,

Petitioner,

against

THE SPERRY CORPORATION, STANDARD CAPITAL COMPANY, J. CHEEVER COWDIN, GEORGE N. ARMSBY, THOMAS A. MORGAN, LINDSAY HOPKINS, EDWARD ALLEN PIERCE, individually and as directors and voting trustees, etc., ALEXANDER B. ROYCE and JOHN SANDERSON, individually and as directors, etc., THOMAS B. DOE, HERBERT H. THOMPSON, individually and as officers, etc., and CHARLES J. GLORE, J. RUSSELL FORGAN, WRIGHT DURYEA and others, individually and as partners trading under the firm name and style of FIELD, GLORE & COMPANY,

Respondents.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

BRIEF FOR THE RESPONDENTS IN OPPOSITION

ARTHUR H. DEAN,
FRANK J. BERBERICH,
Counsel for Respondents Forgan, et al.

HENRY A. MULCAHY,
Of Counsel to
CHADBOURNE, HUNT, JAECKEL & BROWN,
Attorneys for Respondents Standard Capital Co. and Cowdin.

ISIDOR WASSERVOGEL,
GEORGE SYLVESTER,
Counsel for Respondents Morgan, Sanderson & Doe
and for
SKUTCH & BURTON,
Attorneys for Respondent Pierce.

E. W. DEBEVOISE,
Counsel for
DEBEVOISE, STEVENSON, PLIMPTON & PAGE,
Attorneys for Respondent Royce.

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IN THE

Supreme Court of the United States

OCTOBER TERM 1945

No.

JULES E. PICCARD, on behalf of himself and for the benefit of and on behalf of the defendant, THE SPERRY CORPORATION, and all other stockholders of said defendant, THE SPERRY CORPORATION, who may be similarly situated,

Petitioner,

against

THE SPERRY CORPORATION, STANDARD CAPITAL COMPANY, J. CHEEVER COWDIN, GEORGE N. ARMSBY, THOMAS A. MORGAN, LINDSAY HOPKINS, EDWARD ALLEN PIERCE, individually and as directors and voting trustees, etc., ALEXANDER B. ROYCE and JOHN SANDERSON, individually and as directors, etc., THOMAS B. DOE, HERBERT H. THOMPSON, individually and as officers, etc., and CHARLES J. GLORE, J. RUSSELL FORGAN, WRIGHT DURYEA and others, individually and as partners trading under the firm name and style of FIELD, GLORE & COMPANY,

Respondents.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

---

BRIEF FOR THE RESPONDENTS IN OPPOSITION

Opinions Below

The opinion of the District Court (Rifkind, D. J., R. 863-872) is reported in 48 F. Supp. 465. The opinion of the Circuit Court of Appeals (R. 897-898) is reported in 152 Fed. (2d) 465.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered January 10, 1946 (R. 899). The petition for a writ of certiorari was filed April 8, 1946. The jurisdiction of this Court is invoked under Section 240(a), as amended (28 U. S. C. A., Sec. 347a).

Questions Presented

The only questions presented by the petition for a writ of certiorari are:

Did the Circuit Court of Appeals, in unanimously affirming the decision of the District Court, decide (a) an important question of local law in conflict with applicable local decisions; or (b) a Federal question in conflict with applicable decisions of this Court.

Outline of the Case

This is not the conventional derivative suit. Here the defendant directors of the Sperry Corporation, long before stockholders interceded, vigorously asserted the claim involved against the defendant Cowdin, a fellow director; demanded the return of an alleged improper profit; and obtained substantial restitution without litigation or expense (R. 883-887).

The controversy among the Sperry directors arose out of the sale by the defendant Field, Glore & Company, under an option, of a substantial block of stock held by Sperry in the Curtiss-Wright Corporation. The defendant Cowdin, a Sperry director and a leading figure in the aviation industry (R. 164, 403, 405, 525), arranged the transaction with Field, Glore and, as president of Standard Capital Company, rendered substantial service in the sale of the stock (R. 882). For its efforts, Field, Glore had ceded to

Standard Capital a 50% interest in their profits (Plff.'s Ex. 4), on the express condition, however, that the participation be disclosed to and approved by the Sperry directors (Finding No. 35; R. 835). At the time of the transaction (September, 1935), Sperry had been attempting to dispose of its Curtiss stock for almost two years without appreciable success (R. 876) and no one believed that Field, Glore would succeed (R. 550, 658) or that there would be profits (R. 193, 195, 224, 526).

Cowdin disclosed to the Sperry directors that he expected a company in which he was interested would participate in Field, Glore's profits but did not inform them of the extent of its interest (R. 878). His position was that while a 50% participation had been suggested, no definitive agreement had actually been made on September 19, 1935, when the option was approved by the Sperry directors (R. 476).

A runaway market in aviation securities, commencing late in December, 1935 (R. 477; Ex. 80-A, p. 854; Ex. 80-B, p. 856; 882), resulted in profits beyond the expectations of any of the parties involved.

The Sperry directors insisted that Standard Capital was not entitled to its share of the profits (R. 883) because of Cowdin's failure fully to disclose the *amount* of its interest (R. 883). Cowdin violently disagreed (id., R. 477). In the settlement ultimately made, Standard Capital restored to the Sperry Corporation $101,407 (R. 887).

The following figures will exemplify how advantageous a settlement this was. The total profit amounted to $528,000. Under the option agreement, Field, Glore was first entitled to retain $1 per share profit on 82,582 shares of Class A, or $82,582, and 50¢ per share profit on 329,951 shares of common, or $165,976, making a total of $247,000 to be retained by Field, Glore. Deducting this amount from the total profit of $528,000, there remained $281,000 to be divided equally between Sperry and Field, Glore. It was on this basis that Field, Glore originally accounted to Sperry, sending to the Sperry Company their checks aggregating $140,864.08 (Plff.'s Ex. 13; R. 751).

Thus total profits were apportioned as follows:

Sperry	$140,864
Field, Glore	193,935
Standard Capital	193,935
	$528,734

As a result of the settlement, total profits were reapportioned as follows:

Sperry	$277,271
Field, Glore	158,935
Standard Capital	92,528
	$528,734

The option agreement had given Sperry an equal participation with Field, Glore in profits in excess of the minimum to be retained by Field, Glore for their services. As has been indicated, an unexpectedly favorable market developed for aviation securities. That favorable market produced additional profits of $281,000, of which Sperry was to have received one-half or approximately $140,000. The settlement, however, gave Sperry $277,000 or over 98% of these profits. Sperry got substantially the entire profit resulting from the favorable market. These figures portray better than can words that this was an arm's length negotiation in which the Sperry directors recovered for their company an amount which probably exceeded any net recovery that could have resulted from the most successful litigation.

The record, therefore, overwhelmingly established that the Sperry management rendered the corporation intelligent and farseeing service in consummating the settlement here attacked. Their wisdom in accepting restitution of more than half of the claimed improper profits, without loss of time or effort, and without litigation or expense, is an instance of the sound practical judgment of directors which has consistently received judicial approbation and has never been interfered with by courts.

Judge Rifkind, in his opinion, stated (R. 872):

> "It is not to the discredit of the defendant directors that they did not wait for the prod of minority stockholders but vigorously asserted the corporation's claim against their fellow director and obtained a settlement which, in view of the difficult issue of fact and the uncertainty attending all litigation, is fair."

The Questions of Law

Essentially, the questions which are sought to be presented to this Court are:

1. Whether, under applicable local decisions, despite findings that Field, Glore acted in good faith, Field, Glore was liable for participation in a breach of trust, or was in a fiduciary relationship to Sperry and breached a fiduciary obligation;

2. Whether the provision of the charter of the Sperry Corporation, authorizing an interested director to be counted for purposes of a quorum, was valid under Delaware law?

1. It will be established, as the District Judge found, that Field, Glore acted in good faith throughout; that there was no fiduciary relationship between Field, Glore and the Sperry Corporation; and that, in no event, is there any question of law warranting the consideration of this Court.

2. It will be demonstrated further that the provision in the charter of the Sperry Corporation, referred to by appellant, was perfectly valid, as the authorities fully established. There is no decision or statute in Delaware, prohibiting the stockholders of a corporation from consenting to participation by interested directors in corporate transactions. But, in any event, this provision was wholly unnecessary to the Court's decision. Whether or

not there was an interested quorum, a transaction which is fair and reasonable under all the circumstances will be sustained (*Pepper* v. *Litton*, 308 U. S. 295, and cases cited below).

ARGUMENT

I

In affirming the dismissal of the complaint as to Field, Glore, the Circuit Court of Appeals acted in accordance with applicable local decisions.

A

On findings based on undisputed evidence Field, Glore was properly held not to be liable for participation in a breach of trust.

In negotiations with Cowdin, Forgan of Field, Glore told him that the participation by Standard Capital in their profits must be disclosed to and be approved by the Sperry board of directors and by the New York Stock Exchange, and Cowdin agreed to the making of such disclosure (Finding No. 35; R. 880). Field, Glore instructed its counsel to collaborate on the preparation of the definitive agreement and to see to it that proper disclosure of the Standard Capital participation was made to the Sperry board (Finding No. 36; R. 880). Sperry's counsel told Field, Glore's counsel that a proper disclosure had been made by Cowdin and that a disinterested majority of the Sperry board had approved (Finding No. 38; R. 880). Field, Glore informed the Stock Exchange of the option agreement, of the arrangement with Standard Capital and that Field, Glore had been advised that the participation of Standard Capital had been communicated to the Sperry board (Finding No. 40; R. 881). Field, Glore believed that Sperry knew and had approved of Standard Capital's participation (Finding No. 41a; R. 881).

These findings compelled the conclusion reached by the Trial Court that Field, Glore "executed the September, 1935 agreement in good faith and in the reasonable belief that the facts concerning the participation of Standard Capital Company had been disclosed to and approved by the directors of the Sperry Corporation" (Conclusion No. 7; R. 888).

On these facts, Field, Glore clearly was not liable for participation in a breach of trust under applicable local decisions. The rule as to the liability of one dealing with a fiduciary is concisely stated in *Wechsler* v. *Bowman*, 285 N. Y. 284, 291:

> "Anyone who *knowingly* participates with a fiduciary in a breach of trust is liable for the full amount of the damage caused thereby to the cestui que trust." (Italics supplied.)

Petitioner disregards the essential qualification in this rule that the person to be charged must *knowingly* participate. That qualification is explicit in other statements of the rule.

> *Jackson* v. *Smith*, 254 U. S. 586, 589;
> *Irving Trust Company* v. *Deutsch*, 73 Fed. (2d) 121, 125.

The language adopted in the Restatement of the Law of Restitution, Section 138(2), expresses the same qualification in equivalent language. A duty of restitution is imposed only where a third person has "colluded with a fiduciary in committing a breach of duty".

Here the findings, fully supported by the testimony, establish that Field, Glore did not *knowingly* participate with Cowdin in any breach of trust. On the contrary, Field, Glore consented to a participation in its profits by Standard Capital on the express condition that the participation be disclosed to and approved by the Sperry Directors. The option agreement was made and the participation granted to Standard Capital only after assurance was received that the participation was fully disclosed to and approved by the Board of Directors of Sperry.

B

The Courts below properly found that Field, Glore was not in a fiduciary relationship to Sperry and did not breach any duty owed to that corporation.

Field, Glore was a partnership engaged in the investment banking business and a member of the New York Stock Exchange (Finding No. 11; R. 875). None of the Field, Glore partners was an officer, director or voting trustee of Sperry (Finding No. 12; R. 875). In January of 1935, Sperry placed with Field, Glore an order to sell 90,000 shares of Curtiss-Wright "A" stock at a minimum price of $10 a share. No stock was sold on this order since the market price never reached $10 a share before the order was cancelled by Sperry in September, 1935 (Finding No. 21; R. 876). The January sell order was cancelled on September 19, 1935 (R. 739), and the option agreement was not executed until September 25, 1935 (Finding No. 30; R. 878).

On these facts, the Trial Court concluded that there was no fiduciary relationship between Field, Glore and Sperry (Conclusion No. 6; R. 888). Petitioner's attack on this holding ignores both the law and the facts.

A stockbroker, of course, is an agent, and within the scope of his agency subject to all the normal duties of an agent to his principal. But agency does not create an unchangeable status. It does not prevent an agent from thereafter dealing with his principal or from profiting from a transaction which is outside the scope of his agency. As emphasized in *New York Trust Co.* v. *American Realty Co.*, 244 N. Y. 209, 216, the profits and advantages which an agent may not derive at the expense of his principal are *those* which are the "fruit of the agency" obtained "in the execution of the agency".

Field, Glore had properly performed under the January sell-order. It had kept its principal advised of its inability to perform the specific task imposed. No sales were made since the market never reached the specified price. "Once an

agent to sell has ended his agency through proper performance, he is, of course, free of all obligations" (concurring opinion of Frank, J., in *Shultz* v. *Manufacturers & Traders Trust Co.*, 128 Fed. (2d) 889, 899).

Petitioner's argument that Field, Glore was in a fiduciary relationship to Sperry ignores the fact that the January sell order was cancelled before the option agreement between Sperry and Field, Glore was entered into. The case of *Johnson* v. *Winslow*, 155 Misc. 170, affirmed 272 N. Y. 467, relied on by petitioner (Brief, p. 14) clearly recognized that where notice of a change of relation from that of broker and customer to that of dealer and customer is made clear, the former broker may properly purchase for himself the securities of his customer.

Sperry was aware of the fact that it was entering into a new and different arrangement with Field, Glore. Under the option agreement Field, Glore was plainly a purchaser of the stock (see *Lonsdale* v. *Speyer*, 174 Misc. 532, 546, 547, 550; aff'd 259 App. Div. 802; aff'd 284 N. Y. 756). The Courts below have therefore properly concluded that there was no fiduciary relationship between Field, Glore and Sperry.

Even if Field, Glore had been under a fiduciary duty as an agent to Sperry, on the undisputed facts as found, Field, Glore was not guilty of any breach of duty. Its own interest was fully disclosed and it was advised that a proper disclosure had been made by Cowdin and that a disinterested majority of the Sperry Board had approved (Finding No. 38; R. 880). The Restatement of the Law of Agency, Section 390, makes it clear that the duty of an agent to communicate to his principal all material facts in connection with a transaction is not unqualified. The duty exists "unless the principal has manifested that he knows such facts or that he does not care to know them". In comment "b" to this section the qualification is explicitly stated as follows:

> "These statements are subject to the limitation that if the principal manifests that he knows all material facts

> or is willing to deal without knowing them, the agent is not liable if he fails to reveal them."

See also Restatement of the Law of Restitution, Section 191, subdivision (2).

Here the Courts below have found that Field, Glore believed that Sperry knew and had approved of Standard Capital's participation (Finding No. 41a; R. 881) and that Field, Glore executed the option agreement "in good faith and in the reasonable belief that the facts concerning the participation of Standard Capital Company had been disclosed to and approved by the Directors of the Sperry Corporation" (Conclusion No. 7; R. 888). On these facts the Court could not have found that Field, Glore breached any duty owed by it to Sperry even if the existence of a fiduciary relationship be assumed. The complaint was therefore properly dismissed.

II

The settlement was made in good faith and was valid. Therefore, the releases delivered by Sperry and Sperry Securities Corporation to Standard Capital Company and Cowdin are valid and binding.

The Sperry charter (Par. 10) provided that a director shall not be deemed interested, solely by reason of stock ownership in a company contracting with Sperry. Petitioner contends that this provision was invalid. There is no merit to that contention. Nor need that question be determined here.

The Court below held, not only that Paragraph 10 of the Charter was valid, but that the settlement was fair and made in good faith (Finding No. 73; R. 887); and was, in any event, approved by a majority of disinterested directors, constituting a quorum (R. 884, 886, 871). Based on this and other findings, the Court below concluded that the releases delivered to Standard Capital Company and Cow-

din are valid and binding (Conclusion No. 8; R. 888). In view of these findings, the validity of the charter provision involved need not be considered.

(1) It is well established that the conflicting interest of one or more corporate directors is not alone sufficient to render their action void. It requires only that the Court scrutinize their action with care and determine whether it was fair under all the circumstances.

Twin Lick Oil Co. v. *Marbury*, 91 U. S. 587, 589;
Pepper v. *Litton*, 308 U. S. 295;
Geddes v. *Anaconda Copper Mining Co.*, 254 U. S. 590, 599;
Corsicana National Bank v. *Johnson*, 251 U. S. 68, 90;
Cowell v. *McMillen*, 177 Fed. 25, 39 (C. C. A. 9th).

In the absence of proof of unfair dealing, the courts have uniformly approved corporate transactions, even where some or all of the individual directors represented seriously conflicting interests.

Crawford v. *Mexican Petroleum Co. of Delaware*, 130 Fed. (2d) 359 (C. C. A. 2d 1942);
Blaustein v. *Pan American Petroleum Co.*, 293 N. Y. 281, 298;
Everett v. *Phillips*, 288 N. Y. 227, 236;
Chelrob Inc. v. *Barrett*, 293 N. Y. 442, 460.

The Delaware courts are in accord with the rule that the interest of a director in a corporate transaction does not of itself render the transaction void. Bad faith or overreaching must be established.

Potter v. *Sanitary Co.*, 22 Del. Ch. 110; 194 Atl. 87, 91;
Eshelman v. *Keenan* (Del. Ch.) 2 Atl. (ad) 904, 908.

Consequently, even if Paragraph 10 of the Sperry Charter were invalid, the finding that the settlement was fair and made in good faith is conclusive upon the issues of this case.

(2) In any event, the settlement was in fact approved by a majority of disinterested directors constituting a valid quorum, without regard to the Charter provision. During the relevant period, there were eight Sperry directors: Morgan, Sanderson, Pierce, Royce, Doe, Cowdin, Armsby and Hopkins (R. 884; 886). Under the By-Laws a quorum consisted of a majority of the directors then in office, not less than two (R. 689). When the settlement was ratified, at the Sperry board meeting on July 28, 1936, all eight directors were present. The settlement was approved by all except Cowdin and Armsby, who did not vote. Whatever law were applicable, five directors would constitute a quorum and if they took unanimous action would, of necessity, constitute a majority at any meeting. Unquestionably, Doe, Hopkins, Pierce, Royce and Sanderson were disinterested. Ratification, therefore, was valid without reference to the Charter.

But Morgan, as well as Sanderson, was disinterested. At the time of the meetings, Morgan and *Mrs.* Sanderson each owned 50 shares of common and 50 shares of preferred stock of Standard Capital Company, for which each paid $5,050. Standard Capital Company had outstanding at the time 10,555 shares of common and 4,750 shares of preferred. Therefore, Morgan and Mrs. Sanderson each owned ½ of 1% of the common and 1% of the preferred stock of Standard Capital Company.

This inconsequential stock interest of Morgan does not constitute a disqualification under the authorities. Sanderson certainly was not disqualified by his wife's stock interest acquired with her own independent means (R. 276, 360, 871).

As to Morgan, it is well settled that a nominal stock interest is not disqualifying (*Sage* v. *Culver*, 147 N. Y. 241, 247; *Michoud* v. *Girod*, 4 How. (U. S.) 503, 554; *Restatement of the Law of Restitution*, Sec. 192; *Restatement of the Law of Trusts*, Sec. 170, pp. 432-3; 29 Columbia L. Rev. 338, 342).

As to Sanderson, the District Judge ruled that Sanderson's vote cannot be disregarded because, as the District Judge found, "The evidence does not suggest that Sanderson was the beneficial owner of his wife's stock. No one testified that Sanderson held the stock in his wife's name or that it was bought with Sanderson's funds. * * * The evidence does not support the contention that he was an interested director" (R. 871).

In sum, the Court below held that in settling the controversy with Standard Capital Company and Cowdin, the action of the directors was attended by "good faith, sound business judgment and prudent solicitude for the welfare of the corporation" (R. 865). The Courts have repeatedly held that a settlement thus made is binding and may not be set aside because a minority stockholder disagrees with the judgment of the directors.

Corbus v. *Gold Mining Co.*, 187 U. S. 455, 463;
Mendelson Bros. v. *Sachs*, 253 App. Div. 270, aff'd 279 N. Y. 604;
Continental Insurance Co. v. *N. Y. & H. R. R. Co.*, 187 N. Y. 225;
Kirchner v. *N. H. S. M. Co.*, 135 N. Y. 182, 188;
Holland v. *Presley*, 225 App. Div. 667, 669, aff'd 280 N. Y. 835.

(3) Moreover, paragraph 10 of the Charter is valid. Nothing contained in the Charter clause in question is in conflict with any statutory prohibition or with any public policy of the State of Delaware. Stockholders or the beneficiaries of any trust may consent "that the trustee shall act under conditions of divided loyalty."

Chandler v. *Bellanca Aircraft Corp.* (Del. Ch.), 162 Atl. 63, 67;
Matter of Balfe, 245 A. D. 22, 24 (2nd Dept.);
Butterfield v. *Cowing,* 120 N. Y. 486;
Everett v. *Phillips,* 288 N. Y. 227;
Voigt v. *Remick,* 260 Mich. 198, 244 N. W. 446;
Helfman v. *American Light & Traction Co.,* 121 N. J. Eq. 1, 187 Atl. 540;
Spiegel v. *Beacon Participations,* 297 Mass. 398, 417, 8 N. E. (2d) 895;
Restatement of the Law of Trusts, Sec. 216;
Restatement of the Law of Restitution, Sec. 191.

The Delaware cases, relied on by appellant for a contrary view, are not in point—no provision of the certificate of incorporation was involved.

This charter clause affords no greater latitude to a director than does a clause authorizing directors to act in matters where they have conflicting interests; and the cases are legion in which the validity of charter clauses authorizing "interested" directors to act have been sustained.

Everett v. *Phillips,* 288 N. Y. 227;
Chelrob Inc. v. *Barrett,* 293 N. Y. 442;
Spiegel v. *Beacon Participations, Inc.,* 297 Mass. 398, 8 N. E. (2d) 895;
Helfman v. *American Light & Traction Co.* (N. J. Ch.), 187 Atl. 540;
Voigt v. *Remick,* 260 Mich. 199, 244 N. W. 466.

Therefore, even if the stock interest of Morgan and Mrs. Sanderson in Standard Capital Company could under any circumstances be said to constitute a disqualification, the charter clause in question precludes that inference.

In any event, there is nothing for this Court to review.

CONCLUSION

The decision below is in accord with applicable local decisions and it is not in conflict with applicable decisions of this Court. It is, therefore, respectfully submitted that the petition for a writ of certiorari should be denied.

ARTHUR H. DEAN,
FRANK J. BERBERICH,
Counsel for Respondents Forgan, et al.

HENRY A. MULCAHY,
Of Counsel to
CHADBOURNE, HUNT, JAECKEL & BROWN,
Attorneys for Respondents Standard Capital Co. and Cowdin.

ISIDOR WASSERVOGEL,
GEORGE SYLVESTER,
Counsel for Respondents Morgan, Sanderson & Doe
and for
SKUTCH & BURTON,
Attorneys for Respondent Pierce.

E. W. DEBEVOISE,
Counsel for
DEBEVOISE, STEVENSON, PLIMPTON & PAGE,
Attorneys for Respondent Royce.

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IN THE

Supreme Court of the United States

OCTOBER TERM 1945—No. 1086

JULES E. PICCARD, on behalf of himself and for the benefit of and on behalf of the defendant, The Sperry Corporation, and all other stockholders of said defendant, The Sperry Corporation, who may be similarly situated,

Petitioner,

against

THE SPERRY CORPORATION, STANDARD CAPITAL COMPANY, J. CHEEVER COWDIN, THOMAS A. MORGAN, EDWARD ALLEN PIERCE, individually and as directors and voting trustees, etc., ALEXANDER B. ROYCE and JOHN SANDERSON, individually and as directors, etc., THOMAS B. DOE, individually and as officers, etc., and J. RUSSEL FORGAN, WRIGHT DURYEA and others, individually and as partners trading under the firm name and style of FIELD GLORE & COMPANY,

Respondents.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals, Second Circuit.

REPLY BRIEF FOR PETITIONER

A. JOSEPH GEIST,
Attorney for Petitioner.

GEORGE E. NETTER,
HELEN M. WOLFSOHN,
of Counsel.

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Respondents.

REPLY BRIEF FOR PETITIONER

I

As to Defendants Field Glore & Company.

A. Field Glore was in a fiduciary relationship to Sperry.

Field Glore seek to escape from their fiduciary obligations by stating that the selling order to them as brokers was cancelled on September 19, 1935, and that the option agreement was not executed until September 25, 1935 (Brief, pp. 8, 9). This is a misconception of the facts.

Field Glore were concededly fiduciaries as brokers under the sell order. To accomplish their purpose to convert the sell order into the form of an option (656, 658, 660, 662), they agreed to give their principal's voting trustee, director and representative an unusually large participation in the profits, but failed to disclose that fact to their principal.

In the latter part of August or early September, while the sell order was still in effect and admittedly Field Glore were fiduciaries, Cowdin and Field Glore talked about a 50% participation and "came to an agreement on it very quickly" (445-454). The trial judge found that at the September 19 meeting, at which the Sperry directors authorized the cancellation of the sell order and approved the option agreement, Cowdin reasonably expected that the share of his company in the Field Glore profits would be approximately 50%, but falsely represented that the participation would be a small one (2632; Finding 26). Such participation, therefore, must have been arranged between Cowdin and Field Glore before the meeting, when Field Glore were concededly fiduciaries under the sell order. Field Glore violated their fiduciary obligation by failing to make full and true disclosure of the arrangement with Cowdin.

While they were admittedly fiduciaries, Field Glore arranged a deal with their principal's trustee, Cowdin. By that deal Field Glore received an option on the stock, and Cowdin was given a 50% share in the profits of the option, which was to be paid not to him, but to his corporation. As part of the same deal, the sell order to Field Glore as brokers was cancelled. All this was not fully and truly disclosed, but, on the contrary, Cowdin was permitted, by the negative action of Field Glore, to make a false representation as to the extent of his interest.

Duryea of Field Glore testified that the sell order "was converted into an option arrangement" (660) and that Field Glore "had been trying to get it in the form of an option" (662). He also testified "the principal problem of

both Cowdin and Armsby" "was trying to get the Board to agree on the concentration of the sale of the Curtiss-Wright stock in one place, and also to get them to agree to an option form of selling rather than what I considered the rather foolish method they had employed up to that time" (658). Cowdin advised the Sperry directors that "to get the best *services of a broker in doing the selling* such broker should have an option during the period" (2382; emphasis supplied).

Moreover, the option contemplated "resales" of the stock by Field Glore and a division of profits between Field Glore and Sperry (2226-2231). Field Glore charged brokerage commissions under the option agreement (2231, 544). That Field Glore and Sperry were jointly interested in the profits which would result from the resale of the stock was in itself sufficient to make Field Glore fiduciaries.

Silverman v. *Bob* (1st Dept.), 253 App. Div. 303, 2 N. Y. Supp. (2d) 121;
May v. *Hettrick*, 181 App. Div. 3, 167 N. Y. Supp. 966, aff'd 226 N. Y. 580.

B. Field Glore violated its fiduciary duty to Sperry and knowingly participated with Cowdin in the breach of his trust.

It was evidently the theory of the courts below that Field Glore's belief that Sperry knew and had approved of Standard Capital's participation was sufficient to exonerate Field Glore of any responsibility in the matter and that they were under no positive duty to see to it that full, fair and unequivocal disclosure was made to Sperry (2642, 2663; Finding 41a, Conclusion of Law 7). Petitioner contends, however, that on the admitted facts in this case Field Glore were charged with the positive duty of seeing to it that Sperry was fully and correctly informed. That is the crux of the case against Field Glore.

The courts below have created a dangerous precedent by fixing a low standard of conduct for Field Glore. Even the ethics of the market place have been violated, and

certainly the high standards heretofore established for fiduciaries and those dealing with fiduciaries have not been lived up to. This lowering of the bars, against which our great chancellors have heretofore eloquently warned, may result in a dangerous trend unless corrected by this court. (See *Meinhard* v. *Salmon*, 249 N. Y. 458, 464.) Hence, the extreme importance of this court taking jurisdiction.

Field Glore, knowing that Cowdin was Sperry's fiduciary, agreed to pay him a finder's or intermediary's commission (1312, 1475, 599) in the unusual amount of 50% of the profits resulting from the option which he obtained for them from Sperry. They agreed to pay this, not frankly and openly to Cowdin, but to his corporation, Standard Capital, which had "no responsibility or financial undertaking" in the matter (2484).

Even if Field Glore were so naive as to believe that Cowdin had fully disclosed to the directors the 50% participation in the name of Standard Capital, Field Glore were nevertheless aware that the true transaction was one which the Sperry directors as fiduciaries should not and could not approve.

> "Their act in so doing was within their corporate power, but the manner in which they exercised that power, and the amounts which they allowed, were such that their acts were in violation of their duties as fiduciaries." *Griffin* v. *Smith* (C. C. A. 7), 101 F. (2d) 348.

See also:

> *Landes* v. *Hart* (1st Dept.), 131 App. Div. 6, 115 N. Y. Supp. 337, quoted from at page 13 of our Brief in Support of Petition for Certiorari;
> *Keenan* v. *Eshleman*, 23 Del. Ch. 234, 2 Atl. (2d) 904.

Had Cowdin been acting for an individual principal, Field Glore might have been exonerated from responsibility if that principal had manifested either that he

knew all the facts or that he did not care to know them. However, the Sperry directors were themselves fiduciaries, not principals.

Moreover, there is nothing in the record to support the assertion that Sperry, or even its directors, manifested to Field Glore that it knew all the material facts. On the contrary, the record establishes that Field Glore did not believe that Sperry knew the essential fact that the participation by Cowdin's company was as much as 50% and was not a small participation.

Field Glore readily entered into the subterfuge whereby Cowdin took the 50% participation in the option profits, not in his own name, but in the name of his corporation, Standard Capital, of which Forgan of Field Glore was a director (454-457, 425). Although Field Glore knew that Cowdin, a director and voting trustee of Sperry, was acting for Sperry and was its sole representative, Forgan of Field Glore testified that Cowdin made it "very clear" that "so far as any profit was concerned" he brought the business to Field Glore "as an officer of Standard Capital" (455).

It was unnecessary for Field Glore to indulge in assumptions as to whether full disclosure had been made. They could have been assured of this by sending Sperry a letter stating that Standard Capital was getting 50% of the profits, as they did to the New York Stock Exchange; but they did not (Ex. 8; 2244-2245). Field Glore sent Standard Capital a copy of the letter to the Stock Exchange which was unnecessary, but did not send Sperry a copy, although they definitely should have done so in modicum discharge of their fiduciary obligation (2220, 2224, 604). Field Glore asked Cowdin whether he had any objection to their stating to the Stock Exchange what Standard Capital's interest was (1320-1321). Even the letter to the Stock Exchange did not disclose that Cowdin, the principal stockholder of Standard Capital, had represented Sperry in negotiating the option (2244-2245).

Although they wrote to the Stock Exchange, Field Glore connived at Cowdin's fraud on Sperry. Indeed, *the letter to the Stock Exchange is cogent evidence that Field Glore did not believe that Standard Capital's 50% participation in the profits had been disclosed to Sperry.* Field Glore specifically informed the Stock Exchange that "we propose to cede to Standard Capital Company an interest of 50% of our share of the net profits" (2244-2245); but were careful not to say that it had been disclosed to Sperry that the participation was 50%. In cautiously chosen language, they wrote merely that "We are advised that the fact that the Standard Capital Company may participate in our share of the net profits on this transaction has been communicated to the Board of Directors of Sperry Corporation" (2245).

The artful language of this letter is virtually an admission that Field Glore knew that Cowdin had not made full disclosure of his 50% participation. Indeed, even in their brief here respondents do not contend that Field Glore believed that Cowdin had disclosed to Sperry a participation of as much as 50% in its profits.

It is argued by respondents that Sperry's counsel told Field Glore's counsel that a proper disclosure had been made by Cowdin (Brief, p. 6). However, defendant Royce, counsel for Sperry, did not say what disclosure had been made and Field Glore's counsel did not say what were the facts which should have been disclosed, nor call attention to the important fact that the interest of Cowdin's company, Standard Capital, was in the abnormally large amount of 50% and not a mere small participation (1529-1531, 1537, 1541-1542, 2517).

II

As to Cowdin's Alleged Services.

Respondents' assertion that Cowdin rendered substantial services in the sale of Curtiss-Wright stock (Respondents' Brief, p. 2) is not supported by the record. The trial judge found merely that "Cowdin rendered some services in promoting the sale of the Curtiss-Wright stock" (2644; Finding 47). He also found that pursuant to a resolution adopted by the directors of the Sperry Corporation in September, 1934, Cowdin received a salary of $1,000 a month for services in connection with Sperry's investment in Curtiss-Wright stock; that Cowdin performed such services; and that the payments were discontinued by order of the board at the end of February, 1936 (2629; Finding 23). The resale of the stock under the option had been completed by February, 1936. Moreover, as also found by the trial judge, beginning the latter part of 1935 and continuing to the spring of 1936, there was a stock market boom in aviation stock, including Curtiss-Wright (2644; Finding 45). In the light of this boom, Cowdin's services in promoting the sale of the stock could not have been very important.

It is unmistakable on the record that the participation in the profits by Cowdin's company was an "originating" or "finder's commission" for procuring the option for Field Glore (1312, 599).

III

The Releases to Cowdin and Standard Capital Are Not Valid Corporate Acts.

While the interest of a director in a transaction with his corporation renders that transaction voidable, not absolutely void, the transaction nevertheless requires the valid action of a proper quorum of the corporation's directors. Sperry's charter specifically provides that a transaction with an interested director must be approved or ratified by the affirmative vote of a majority of the directors present at a meeting, who are not so interested (2654; Finding 66).

Respondents cite no authority holding valid a charter provision purporting to authorize an interested director to vote or be counted towards a quorum, nor have they refuted our showing that the universal rule is that an interested director may neither vote nor be counted towards a quorum (see Petitioner's Brief, p. 17).

None of the cases cited at page 14 of respondents' brief involved a charter provision purporting to authorize an interested director to vote or to be counted towards a quorum.

In the instant case the directors were all interested because of their possible liability for negligence in approving the original transaction without inquiry as to Cowdin's participation after they were put on notice, and their consequent desire to get the matter disposed of. It is no answer to this that the trial court held them not actually liable for negligence, because it was nevertheless to their interest to get the matter quickly and quietly out of the way to avoid any embarrassing claims against themselves.

Respondents also argue that a nominal stock interest is not disqualifying; but the authorities they cite do not support even that proposition (Respondents' Brief, p. 13).

We need not pause to consider it, because the stock interests of Morgan and Mrs. Sanderson, who each paid over $5,000 for the stock, were real, not merely nominal, and were sufficient to produce the conflict between self-interest and duty which the law prohibits.

Respectfully submitted,

A. Joseph Geist,
Attorney for Petitioner.

George E. Netter,
Helen M. Wolfsohn,
of Counsel.